

**STATE OF MICHIGAN
IN THE SUPREME COURT
APPEAL FROM COURT OF APPEALS
Whitbeck, P.J., Owens and Schuette, J.J.**

SHERRY COMBEN, TREASURER FOR
THE COUNTY OF ANTRIM,

Plaintiff-Appellee,

v

THE STATE OF MICHIGAN, JAY B.
RISING in his capacity as STATE
TREASURER OF MICHIGAN, and THE
MICHIGAN DEPARTMENT OF
TREASURY,

Defendant-Appellants,

and

PURE RESOURCES, L.P., a Texas limited
partnership, DOMINION RESERVES, INC., a
Virginia corporation, WOLVERINE GAS &
OIL COMPANY, INC., a Michigan
corporation, WARD HEIRS BEING:
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WARD DEVINE, ELIZABETH PALMER
DEVINE WISEMAN, MICHAEL EDMUND
DEVINE, SUZANNE LEE DEVINE,
WILLIAM W. DUNN, DAVID W. FAY,
EDWIN R. FAY, PETER W. FAY, ROBERT
A. FAY, ROSAMOND S. FISHER,
FREDERICK T. GOLDING, successor trustee
under the Virginia W. Golding Trust
Agreement dated August 30, 1989, NANCY
HAMILTON, LISA MARRIOTT JONES,

Michigan Supreme Court No. 127212

Court of Appeals No. 248963

Antrim County Circuit Court
No. 02-7860-PS

**DEFENDANTS-APPELLEES
DOMINION RESERVES, INC. AND
WOLVERINE GAS & OIL COMPANY,
INC.'S BRIEF ON APPEAL**

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COUNTER STATEMENT OF QUESTIONS PRESENTED

- I. DO THE STATE OF MICHIGAN, JAY B. RISING IN HIS CAPACITY AS THE STATE TREASURER OF MICHIGAN AND THE MICHIGAN DEPARTMENT OF TREASURY HAVE STANDING TO APPEAL THE DECISION IN THE COURT OF APPEALS AND DID THEY HAVE STANDING TO APPEAL THE DECISION OF THE ANTRIM COUNTY CIRCUIT COURT?**

Trial Court's answer: Did not address

Court of Appeals answer: Did not address

Appellant's answer: Yes

Appellee's answer: Yes

- II. IS AN OIL AND GAS LESSEE'S INTEREST EXEMPT FROM AD VALOREM REAL PROPERTY TAXES BY VIRTUE OF SECTION 15 OF THE SEVERANCE TAX ACT, MCL 205.301 *ET SEQ.* AND THUS NOT SUBJECT TO FORECLOSURE?**

Trial Court's answer: Yes

Court of Appeals answer: Yes it is exempt; whether it is subject to foreclosure is not clearly stated in the opinion.

Appellant's answer: No

Appellee's answer: Yes

- III. IS THE LESSEE OF AN OIL AND GAS LEASE ENTITLED TO NOTICE IN FORECLOSURE PROCEEDINGS UNDER MCL 211.78(5)(e)?**

Trial Court's answer: Did not address

Court of Appeal's answer: Did not address

Appellant's answer: Yes.

Appellee's answer: If exempt, no. If subject to foreclosure, yes.

IV. DOES THE DORMANT MINERAL STATUTE PREVENT FORECLOSURE OF DELINQUENT REAL PROPERTY TAXES ON SEVERED FEE MINERAL INTERESTS?

Trial Court's answer: Yes

Court of Appeal's answer: Yes

Appellant's answer: No

Appellee's answer: No

STATEMENT OF FACTS AND PROCEEDINGS

Appellees Dominion Reserves, Inc. and Wolverine Gas and Oil Company, Inc. concur with the Statement of Facts and Proceedings submitted by the Appellant with certain clarifications.

Appellant describes Dominion and Wolverine as “major holders of severed oil and gas rights in Antrim County.” (Appellant’s Brief, p. 2) The accuracy of that description depends on the definition of “severed oil and gas rights.” Dominion and Wolverine are oil and gas lessees under numerous leases in Antrim County. The lessors on some of these leases are the owners in fee of severed oil and gas rights. Neither Dominion nor Wolverine own in fee severed mineral interests in Antrim County.¹

Appellant characterizes the appeal as involving the relationship between the General Property Tax Authority (GPTA) and the Severance Tax Act as they apply to severed fee interests in oil and gas. (Appellant’s Brief, p. 1) Appellees Dominion and Wolverine assert that the appeal also involves the relationship between the GPTA and the Severance Tax Act and oil and gas lessee’s interests.

The Trial Court’s Decision and Order states that the foreclosure provisions of General Property Tax Act, MCL 211.78-78p, if properly followed do not extinguish severed oil and gas interests, specifically including oil and gas lessee’s interests. (Appellant’s Appendix 19a and 41a) Appellant’s Brief focuses on foreclosure of severed fee interests in oil and gas.

¹ A lessee’s interest is created by an oil and gas lease which grants the exclusive right to the lessee to produce and operate the property for oil and gas. *Energetics v Whitmill*, 442 Mich 38, 47; 497 NW2d 497 (1993). The interest of the lessee is referred to herein as the lessee’s interest. The person owning the mineral rights to which a lease applies will be referred to as owning the fee in the mineral estate or the mineral interest. If the owner of the mineral estate is someone other than the owner of the surface, he would be described as the owner of the severed mineral estate.

In this Brief, Dominion and Wolverine will focus on the question of whether the foreclosure provisions of the GPTA extinguish the oil and gas lessee's interest under a lease that covered the property prior to the time of the tax delinquency, because these are the only interests held by Dominion and Wolverine that are affected by the lower court's decision.

ARGUMENT

I. STANDARD OF REVIEW

Dominion and Wolverine agree with the Appellant that the appropriate standard of review in this matter is *de novo*.

II. THE STATE DEFENDANTS HAVE STANDING TO PROSECUTE THIS APPEAL.

Appellees Dominion and Wolverine adopt as if fully set forth herein the arguments set forth in Section I of Appellant's Brief.

Appellees in support of the State's standing in this matter call the following to the Court's attention: The foreclosure process is intended to aid the State and its political subdivisions in the collection of real property taxes. The State must have standing to participate in a lawsuit of which the sole purpose is to determine the correct interpretation and constitutionality of the statutory provisions governing that process.

The State of Michigan has a right of first refusal to acquire land acquired by foreclosure. MCL 211.78m(1). The State has asserted that the land it acquires when it exercises the right of first refusal includes the mineral fee estate, even if the estate was severed or is covered by an oil and gas lease. (Appellees Dominion and Wolverine maintain that it does not include any interest covered by an oil and gas lease.) The State of Michigan must have standing to participate in an action that will determine the interests in which it has a statutory right of first refusal.

III. THE SEVERANCE TAX ACT EXEMPTS OIL AND GAS LESSEE'S INTERESTS FROM TAXES IMPOSED BY THE GENERAL PROPERTY TAX ACT AND THUS THEY ARE NOT SUBJECT TO FORECLOSURE.

A. An Oil and Gas Lease is an Interest in Real Property.

The owner of the surface estate owns the minerals (including oil and gas) located beneath his land. *Manufacturers National Bank of Detroit v Department of Natural Resources*, 420 Mich

128; 141 NW2d 572 (1984). Surface owners may sever minerals (including oil and gas) from the surface estate by conveyance or reservation. Upon proper severance of legal title to oil and gas there is no continuing unity of title and each estate is a freehold in fee simple. *Van Slooten v Larsen*, 410 Mich 21, 37; 299 NW2d 704 (1980), app dis 455 US 901; 102 S Ct 1242; 71 L Ed 440 (1982).

The owner of the fee simple interest in oil and gas (the surface owner as to unsevered interests or the owner of the severed interest when the oil and gas has been severed from the surface estate) may execute an oil and gas lease. The lessee's interest gives the lessee the right to go upon the surface of the land and extract oil and gas. The lessee's interest in an oil and gas lease is a real property interest. The Michigan Supreme Court has held:

“Notwithstanding Appellant's contention to the contrary, when considered in connection with a controversy of this character, it must be held that a lease of oil and gas rights in a tract of land constitutes an interest in real property, not a mere option We have held that oil and gas are a part of the realty until severed therefrom. [citations omitted] And it follows that a transfer of title or of a right in the unsevered oil and gas, together with the right to go upon the land for the purpose of taking the oil and gas therefrom involves a granting of rights in real estate; and the instruments granting such rights are appropriately denominated ‘leases’.” *Jaenicke v Davidson*, 290 Mich 298, 302 (1939).

As previously stated, Appellees Dominion and Wolverine are oil and gas lessees, and their lessee's interests are the only interests owned by them that are affected by these proceedings.

B. Oil and Gas Lessee's Interests Would Be Subject to Ad Valorem Property Taxes Unless Exempt.

Article IX, Section 3 of the 1963 Michigan Constitution calls for the Legislature to provide for the ad valorem taxation of real property. The Legislature enacted the following statute:

“All property, real and personal, within the jurisdiction of this State, not expressly exempted, shall be subject to taxation.” (emphasis supplied)

MCL 211.1

Thus, the oil and gas lessee's real property interests held by Dominion and Wolverine would be subject to ad valorem real property taxes if not expressly exempted by the Legislature.

C. Oil and Gas Lessees are Obligated to Pay Severance Taxes.

Section 1 of the Severance Tax Act provides:

"Section 1. There is hereby levied upon each corporation, association, or person engaged in the business of severing from the soil, oil or gas, a specific tax to be known as severance tax. Each corporation, association, or person owning, controlling, managing, operating or leasing, in this state, any oil well or gas well, or any such corporation, association or person who produces in any other manner, any oil or gas by taking it from the earth, in this state, shall make monthly, on the first day in each month of each year, a report to the Michigan state tax commission in the form and manner prescribed by such commission showing the total amount of oil or gas produced by such corporation, association or person from each well or otherwise, during the month preceding and the actual market value thereof at the time of production."

MCL 205.301.

The purpose of the oil and gas lease is to allow the lessee to produce and remove (sever from the soil) oil and gas from the leased lands. That is the business of the oil and gas lessee and its responsibility as a prudent operator. The Severance Tax Act obligates the lessee to pay severance tax on its share of the oil and gas produced under its lease.

D. Section 15 of the Severance Tax Act Exempts Owners of Oil and Gas Lessee's Interests from Taxes Imposed by the General Property Tax Act.

Section 15 of the Severance Tax Act exempts those subject to the severance tax from all other taxes using the following language:

"The Severance Tax herein provided for shall be in lieu of all other taxes, state or local, upon the oil and gas, the property rights attached thereto or inherent therein, or the values created thereby; upon all leases or the rights to develop and operate any lands of this state for oil or gas, the values created thereby and the property rights attached to or inherent therein: Provided, however, nothing herein contained shall in anywise exempt the machinery, appliances, pipelines, tanks and other equipment used in the development or operation of said leases, or used to transmit or transport the said oil or gas: And provided further, that nothing herein contained shall in anywise relieve any

corporation or association from the payment of any franchise or privilege taxes required by the provisions of the state corporation laws.” [emphasis supplied]

MCL 205.315.

Appellant argues that the “in lieu of” provision relates only to other taxes on “extracted” oil and gas, i.e. oil and gas “which has been severed from the soil.” Appellant’s Brief, pp. 32, 33. While this argument may be relevant to the question of whether the interest of the fee owner of oil and gas is exempt, it simply ignores the fact that the exemption section describes and specifically exempts from all other taxes, state or local: “ . . . all leases or the rights to develop and operate any lands of this state for oil or gas, the values created thereby and the property rights attached to or inherent therein.” Given this sweeping and unambiguous language, it is impossible to conclude that the exemption in Section 15 does not include ad valorem real property taxes on minerals in the ground, if that conclusion is meant to include the oil and gas lease as an interest in such minerals.

If, as asserted by the Appellant’s Brief, the exemption of the Severance Tax Act is limited to personal property taxes that may be assessed against severed (extracted) oil or gas by the language (including the reference to “leases”) appearing before the proviso in Section 15 with regard to machinery, appliances, pipelines, etc., then there would be no need for the proviso. Clearly in drafting the statute, the legislature intended, when it described the exemption as applying to “. . . all leases on the rights to develop and operate any lands of this state from oil or gas, the values created thereby and the property rights attached to or inherent therein . . .,” that the exemption be applied broadly to all ad valorem taxes that may otherwise have been assessed on such interests. The breadth of the exemption relating to leases and associated development rights made it necessary to identify certain items of personal property that the legislature intended to be taxed. All other property incident to an oil and gas lease was exempted.

The Appellant also argues that “The Legislature did not exempt those subject to the severance tax from all other taxes, state or local. The Act, as the title to its enactment so clearly declares, exempted those paying the tax from certain other taxes, which did not include ad valorem real property taxes on minerals in the ground.” (Appellant’s Brief, pp. 34-35)

The Appellant has continually made this argument to appellate courts of this state only to have it repeatedly and flatly rejected. *Elenbaas v Department of Treasury*, 235 Mich App 372, 597 NW2d 271 (1999) appeal denied, 463 Mich 932, 622 NW2d 63 (2000); *Elenbaas v Department of Treasury*, 231 Mich App 801, 585 NW2d 305 (1998) opinion superseded by *Elenbaas v Department of Treasury*, 235 Mich App 372, 597 NW2d 271 appeal denied, 463 Mich 932, 622 NW2d 63 (2000); *Cook v Dep’t of Treasury*, 229 Mich App 653, 583 NW2d 696 (1998) appeal denied, 463 Mich 932, 622 NW2d 63 (2000); *Cowen v Dep’t of Treasury*, 204 Mich App 428, 516 NW2d 511 (1994) appeal denied, 447 Mich 980, 525 NW2d 450 (1994); *Bauer v Dep’t of Treasury*, 203 Mich App 97, 512 NW2d 42 (1993); appeal denied; 447 Mich 979, 525 NW2d 450 (1994), *Ward Lake Drilling, Inc. v Michigan Department Of Treasury*, Michigan Tax Tribunal Docket No. 231337 (May 16, 1997).

The term “from certain other taxes” only appears in the preamble of the Act and the Court has held that greater deference should be given to the actual statutory language “all other taxes” rather than the preamble, because the preamble is not the authority for construing specific statutory terms.. *Elenbaas I* at 307,

Bauer and its prodigies have continually held that § 15 was clear and unambiguous, and that, when it applies, the severance tax is to be paid in lieu of *all other taxes*. The Appellant has argued repeatedly to the Court of Appeals that *Bauer* was wrongly decided and that Court has

repeatedly rejected the State Defendant's claim. (See *Cook* id, *Ward Lake Drilling, Inc. v Michigan Department Of Treasury*, id) The *Cook* court further held:

In addition, since *Bauer* was decided, the Legislature has had two opportunities to correct *Bauer*'s understanding of the Severance Tax Act if it was contrary to legislative intent. In 1994, the Severance Tax Act was amended to add a provision to help finance the orphan well fund and the state general fund. 1994 P.A. 307, MCL § 205.314(1)(a) and (b); M.S.A. § 7.364(1)(a) and (b), effective October 1, 1994. In 1996, the act was again amended to add a severance tax exemption for certain gas and oil products. 1996 P.A. 135, M.C.L. § 205.303(3); M.S.A. § 7.353(3), effective March 19, 1996. The Legislature is presumed to act with knowledge of appellate court statutory interpretations. *Glancy v Roseville*, 216 Mich App 390, 394, 549 NW2d 78 (1996). We agree with plaintiffs that *Bauer* must be accepted as established law at least in our Court for purposes of these appeals. (*Cook*, at 656)

There can be no question that MCL 205.315 is in lieu of all other taxes. The Severance Tax Act has been determined to create an exemption to such other taxes, such as the Single Business Tax 1975 P A 228, as amended, MCL 208.1 *et seq.* *Cowen*, id, and *Ward Lake Drilling, Inc v Michigan Department Of Treasury*, id, upheld in an unpublished opinion *Ward Lake Drilling v Department of Treasury*, 1999 AWL 33455057 (Mich App, Jan 29, 1999) (NO. 203869), and the State Income Tax Act, MCL § 206.1 *et seq.*; *Bauer* id, *Elenbaas*. It is even more clear that oil and gas lessee's interests are exempt from the ad valorem real property tax as that tax was in existence at the time the Severance Tax Act was enacted.

In *Elenbaas I*, the Court held "[T]he phrase "[t]he severance tax herein provided for shall be in lieu of all other taxes, state or local" is clear and unambiguous. ***The word "all" usually denotes an unqualified classification, leaving no room for exceptions.*** *Elenbaas I* at 307, emphasis added.

Dominion and Wolverine maintain that, based on the line of cases following *Bauer* and the clear language of the statute that the lessee's interest in an oil and gas lease is exempt from any tax other than the severance tax, including ad valorem tax on that interest as real property.

E. Exempt Oil and Gas Lessee's Interests are not Terminated by Tax Foreclosures and Sales Under the General Property Tax Act.

At pages 25 and 26 of its Brief, Appellant argues with regard to the state's interest in severed oil and gas that "severed interests in property are not subject to foreclosure if exempt from taxation under the GPTA." The interest is claimed by Appellant to be exempt because it is "state-owned." As demonstrated above in this Brief, the oil and gas lessee's real property interest under an oil and gas lease is exempt from ad valorem taxation by reason of the "in lieu of" exemption in Section 15 of the Severance Tax Act. Thus, based upon Appellant's arguments that exempt interests are not subject to foreclosure under the GPTA and the precedent cited in Appellant's brief, the exempt lessee's interest under an oil and gas lease is likewise not subject to or affected by foreclosure. It is exemption from tax that matters, not the reason for the exemption.

F. Oil and Gas Lessee's Interest is not Cancelled by Virtue of the Foreclosure of the Lessor's Interest.

This position of the Appellant, set forth for the very first time in Section VI of their brief, is that although exempt from taxation and thus not subject to foreclosure, the oil and gas lessee's interest is somehow "cancelled" if the real property interest of the lessor is foreclosed upon. Appellant's argument is not supported by statute or case law. Both of the cases cited by Appellant in support of this argument are readily distinguishable.

In *Tilchim v Boucher*, 328 Mich 355; 43 NW2d 885 (1956), the Plaintiff was the lessee on a 65-month lease covering certain resort property. The lessor was purchasing the resort property from Defendant Boucher on a land contract. The lessor defaulted on the land contract and Defendant Boucher instituted summary proceedings to forfeit the land contract. A Writ of Restitution was issued terminating the lessor's land contract interest. Plaintiff sued to enforce the lease. The Court, focusing on the fact that the lease was subsequent to the land contract, held

that the lessee's interest was terminated by the land contract forfeiture. *Delose v Bellows—Claude Neon, Co*, 261 Mich 57; 245 NW 569 (1932) involved a mortgage foreclosure on an apartment building with a number of residential leases. The Court held that where the mortgage pre-dated the lease, the lease was terminated at the expiration of the redemption period. These cases support the position that an oil and gas lease which is in effect prior to any tax delinquency would not be terminated by the foreclosure of the lessor's real property interest. Rather, that the person acquiring the interest at tax sale, takes the property subject to the terms of the pre-existing oil and gas lease.

G. Additional Practical Support for the Conclusion that Oil and Gas Lessee's Interests are Exempted from the General Property Tax Act.

The Appellant's assertion that the exemption of Section 15 of the Severance Tax Act is limited to ad valorem property tax that would have been imposed upon the intangible personal property associated with holding the lessee's interest in oil and gas is contrary to the position of the Department of Treasury as stated in Revenue Administrative Bulletin 1989-22, approved April 4, 1989, that provides as follows:

“SEVERANCE TAX IN LIEU OF ALL OTHER TAXES

RAB-89-22. The purpose of this Bulletin is to clarify the provision in the Michigan Severance Tax Act, MCL 205.315, stating in part: '[T]he severance tax herein provided for shall be in lieu of all other taxes, state or local, upon the oil or gas,' . . . The question has come up as to whether or not this exclusion extends to Michigan taxes currently in effect (i.e. the Michigan sales, use and single business taxes). It is the Department's position that this provision extends **only to the ad valorem property taxes** that were in effect at the time the above-referenced section was enacted (1929). If it was the legislature's intent to extend this provision to the sales, use or single business tax, a provision for exclusion would be contained in those individual Acts, all of which were enacted after the exemption provision of the Severance Tax Act.”

Note that there is no attempt by the Department to limit the exemption to ad valorem personal property taxes, as asserted by the Appellant in this action. The State's position in this matter is inconsistent with its own regulations and must be rejected.

H. Response to Questions Raised by the Court in its Order Granting Leave to Appeal.

The Court has asked whether the holder of the lessee's interest in an oil and gas lease is entitled to notice of foreclosure. If the oil and gas lessee's interest is exempt from real property taxes and thus, not subject to foreclosure, then no notice is required. The real property interest of the oil and gas lessee would not be affected by the foreclosure and neither the GPTA nor the standards set forth in *Dow v Michigan*, 396 Mich 192; 240 NW2d 604 (1976) would require notice.

On the other hand, if the Court were to somehow conclude that the oil and gas lessee's interest is subject to foreclosure, then both the GPTA and *Dow* would mandate notice. This result would raise a number of vexing constitutional and statutory questions. What if the Foreclosing Government Unit (FGU) failed to give notice to the oil and gas lessee? The GPTA purports to limit the lessee's remedy to recovery of the fair market value of its property interest. MCL 211.781. Is this provision constitutional? What if the FGU (County) cannot pay? There are oil and gas lessee interests that are more valuable than the entire budget of Antrim County.

It is much more practical to avoid all of these pitfalls and find that the clear language of Section 15 of the Severance Tax Act exempts oil and gas lessee's interests.

IV. THE DORMANT MINERAL ACT DOES NOT APPLY

Appellees Dominion and Wolverine adopt and incorporate by reference Section 10 of the Appellant's Brief. Nothing in the Dormant Mineral Act suggests that it is the exclusive manner in which a severed mineral interest may be terminated. In fact, a severed mineral interest could

be terminated by the foreclosure of a prior mortgage or by a merger with the surface estate. The Dormant Mineral Act simply does not apply to the tax foreclosure issue presented in this matter.

V. THE POSITIONS ADVANCED BY THE AMICI, UNITED CONSERVATION CLUBS ET AL AND THE STATE BAR OF MICHIGAN, REAL PROPERTY LAW SECTION ARE NOT ON POINT

A. The Real Property Section of the State Bar of Michigan

In its brief, the Real Property Section attempts to characterize the position advanced by Appellees Dominion and Wolverine as one of fairness. They say that Dominion and Wolverine argue that it is “unfair” to require the lessee to pay a tax for which it is not responsible. (Dominion and Wolverine disagree with this characterization. They have never discussed fairness, only the fact that a lessee is exempt from taxation). The Real Property Section compares the oil and gas lessee’s situation to that of a mortgagee who may be required to pay real property taxes in order to protect its lien even though that may be “unfair.” This is similar to the point made by the Court of Appeals relating to commercial lessees. There is, however, an obvious difference between an oil and gas lessee on the one hand and a commercial lessee or mortgagee on the other; neither a commercial lessee nor a mortgagee has an interest that is statutorily exempt from real property taxes. Unlike the oil and gas lessees, their property interests are not exempt from real property taxes. The oil and gas lessee’s interest is exempt and the lessee cannot be compelled to pay a tax on property that it does not own in order to prevent the foreclosure sale of tax exempt property that it does own. (Although fairness is not the substance of Dominion and Wolverine’s legal argument, this result is fair to all of the concerned parties.)

The Real Property Section also argues that foreclosure proceedings are “in rem” and that this somehow results in the oil and gas lessee’s interest is subject to foreclosure. Of course foreclosure proceedings are in rem. The issue is what “property” is affected by the in rem

proceeding. Foreclosure of an interest created through a tax delinquency occurring after the date of an oil and gas lease does not affect the prior in time interest. The foreclosure must relate to property (“rem”) that is subject to tax and not to property (“rem”) that is exempt. Arguing that the proceeding is “in rem” misses the point.

B. Michigan United Conservation Clubs (MUCC) et al.

The amicus brief filed by the MUCC does not even attempt to address the question of whether or not an oil and gas lessee’s interest is exempt from real property taxation. Rather, MUCC attempts to persuade the Court that the Natural Resources Trust Fund (NRTF) is threatened by the holding of the Court of Appeals. Dominion and Wolverine believe a reversal of the holding that oil and gas lessee’s interests are exempt from real property taxes would be far more threatening to the NRTF.

The MUCC’s argument seems to assume that the issues with regard to foreclosure on the lessee’s interest are the same as the issues with regard to foreclosure on the fee mineral interest. Nothing could be further from the truth, either with respect to the bases for the claim of exemption or the practical impact of the exemption.

While the exemption claims of the lessee and of the fee mineral owner are based primarily on the Severance Tax “in lieu of” provisions, they are not based on the same language. The fee mineral interest owners base their claim on the provision that the Severance Tax is in lieu of all other taxes on the “oil and gas and the values created thereby.” The State argues that this is a reference to produced oil and gas and not to oil and gas in the ground and yet part of the real estate.

Defendants Dominion and Wolverine acknowledge that the State’s argument may have some validity in this regard, and it is this Court’s responsibility to determine whether or not it does. Defendant Dominion and Wolverine assert no position regarding that argument because it

has absolutely nothing to do with their claim of exemption from tax of their lessee's interests. There can be no argument concerning the meaning of the second clause of the "in lieu of" provisions of the Severance Tax Act. In that clause, the legislature very clearly described the real property interest that is exempted from ad valorem taxation as "... all leases or the rights to develop and operate any lands of this state for oil or gas, the value created thereby and the property rights attached to or inherent therein." This Court can accept the State's arguments concerning the meaning of "oil and gas" in the Severance Tax Statute and yet find the lessee's interest exempt, and, in truth, the State's brief never argues to the contrary.

From a practical standpoint, what the MUCC's argument fails to recognize is that it is the oil and gas lessees who produce oil and gas and pay the royalties that go into the NRTF. Lessees are proud of their role in funding the NRTF and want nothing more than to continue their operations to their benefit and the benefit of the NRTF. If the oil and gas lessee's interest is exempt, and the FGU acquires the mineral fee interest through foreclosure, this is exactly what will happen. If, however, the oil and gas lessee's interests are foreclosed upon, wells will be shut-in or even abandoned. The flow of royalties into the NRTF will be disrupted, to the great detriment of the lessees and the people of the State of Michigan.

CONCLUSION

In summary, the position of Defendants Dominion and Wolverine with regard to the tax exemption stated in Section 15 of the Severance Tax Act is as follows:

Section 15 clearly provides that "[T]he severance tax herein provided for shall be in lieu of all other taxes, state or local, . . . ; upon all leases or the rights to develop and operate any lands of this state for oil or gas, the values created thereby and the property rights attached to or inherent therein: . . ." Defendants Dominion and Wolverine are oil and gas lessees of land included in the tax foreclosure that is the subject of this action. The oil and gas lessee's interests

of Defendants Dominion and Wolverine are real property interests. The value of the lease is the right of the lessee to go upon the property to produce the oil or gas. That value and the property rights attached to the lease are under Section 15 of the Severance Tax Act exempt from ad valorem taxation. This is not a tortured construction of Section 15 based on a convoluted argument. Rather, it is a fair reading of the exemption and accurately reflects the position of the state taxing authorities with regard to the valuation of real property since its enactment.


The state has continuously attempted to whittle away at the plain meaning of the exemption in Section 15 of the Severance Tax Act. The Courts have rebuffed every attempt. Appellees Dominion and Wolverine request that the Court do likewise in this instance and conclude that their lessee's interests are exempt from ad valorem property taxes. If so, the tax foreclosure proceeding cannot terminate their interests.

Exploration and operation of oil and gas wells by oil and gas lessees (including Appellees Dominion and Wolverine) under their oil and gas leases generates the \$33 million of annual revenue that the State has received (Appellant's Brief, p. 6) and applies to worthwhile environment projects under the NRTF. Preservation of exempt leasehold estates from foreclosure under the GPTA will serve to continue that stream of income for the benefit of the State and its citizens.

Respectfully submitted,

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